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FEDERAL COMMUNICATIONS COMMISSION
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August 15, 1996

William F. Caton
Acting Secretary
Federal Communications Commission
Room 222
1919 M St., N.W.
Washington, D.C. 20554

DOCKET FILE COPY ORIGINAL

Re: CC Docket No. 96-149

Dear Mr. Caton:

Sprint respectfully submits its comments in the above-captioned docket. We have also provided Ms. Janice Myles of the Common Carrier Bureau with a diskette containing our comments in Word-Perfect 5.1 format.

Sincerely,

Norina Moy
Director, Federal Regulatory
Policy and Coordination

cc: Janice Myles

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**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

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| In the Matter of |) | |
| |) | |
| Implementation of the Non- |) | CC Docket No. 96-149 |
| Accounting Safeguards of |) | |
| Sections 271 and 272 of the |) | |
| Communications Act of 1934, |) | |
| as amended; |) | |
| |) | |
| and |) | |
| |) | |
| Regulatory Treatment of LEC |) | |
| Provision of Interexchange |) | |
| Services Originating in the |) | |
| LEC's Local Exchange Area |) | |
| _____ |) | |

COMMENTS

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COMMENTS

Sprint Corporation, on behalf of Sprint Communications Company, L.P. and the Sprint local exchange carriers, hereby respectfully submits its comments in response to the Notice of Proposed Rulemaking released July 18, 1996 (FCC 96-308) in the above-captioned proceeding.

I. INTRODUCTION AND SUMMARY

In paragraph 65, the Commission describes the dangers which will attend BOC entry into the interLATA market. It states

[A]fter a BOC affiliate enters competitive markets, that BOC will become subject to the economic incentives of the marketplace and therefore may have an incentive to favor its competitive affiliate or to take actions that could weaken the affiliate's rivals. As

previously noted, a BOC's control of essential local exchange facilities provides a BOC with the opportunity to take these actions. In brief, a BOC could provide inferior service to, charge higher prices to, withhold cooperation from, or fail to share information with its rivals in competitive markets. If a BOC were to provide inferior service to a rival, the quality of the rival's interLATA telecommunications service or information service would be degraded, making the rival less attractive to customers and lowering the prices the rival could charge. If a BOC were to charge higher prices to the rival, the rival would have to charge higher prices to customers and consequently lose market share or accept lower profits. In another example, a BOC could possibly withhold cooperation from an interexchange carrier that needs the BOC's assistance to introduce an innovative new service, until the BOC's affiliate is ready to initiate the same innovative service.

There is little that the Commission can do to alter the economic incentives of a BOC to exploit its local monopoly in the ways described by the Commission. All that regulation can accomplish is to erect structural and other barriers to rein in these incentives. While such barriers -- particularly structural barriers -- are very important, there can be no guarantee that they will be successful in preventing serious discrimination and other harms. The inventiveness of competitors being what it is, and the regulatory process being what it is, it may at least be assumed that in some instances anticompetitive behavior will not

be specifically proscribed and that some violations will go undetected and unpunished.

The chances for effective regulatory enforcement are immeasurably increased if the marketplace itself can be enlisted to prevent the BOC from exploiting its local monopoly to disadvantage competitors. This requires, in turn, that at the time the BOC is permitted to enter the in-region interLATA market in a particular state, it must already face facilities-based, local competition sufficient to deter any attempt by a BOC to support its entry into the interLATA market by raising prices to local customers or by discriminating against its interLATA competitors in their use of local facilities. And, this clearly is what the Telecommunications Act of 1996 intended by requiring that one condition which must precede BOC entry is that the Commission find that the BOC is interconnected within the state for which the authority is sought to "one or more competing providers of telephone exchange service...to residential and business subscribers" and that "such telephone exchange service...[is] offered by such competing providers either

exclusively...or predominantly over their own telephone exchange service facilities...." ¹

It is thus apparent that the Commission is obligated to play a pivotal role in guarding against the behavior mentioned in paragraph 65 though careful examination of a BOC's application for in-region, interLATA authority to make sure that the BOC faces realistic competition sufficient to help curb such behavior. For the Commission to ensure, as it must, under the Section 271(d)(3) entry test that the "public convenience and necessity" will be fostered by BOC in-region interLATA entry, it must find that a combination of marketplace and regulatory tools are available to it.

Sprint firmly believes that it is the administration of the Section 271(d)(3) entry test which is of primary importance. The Commission's regulatory enforcement efforts which come afterward -- while very important -- are secondary.

As for regulatory enforcement, by far the most important safeguard is structural separation. Section 272(a)(2)(A) precludes a BOC from providing in-region, interLATA

¹ It is Sprint's understanding that requests have been made of the BOCs in all states and that there will be no "failure to request access" under §272(c)(1)(B).

telecommunications service (at least for three years), except through a separate affiliate. Although Section 272 contains some guidance, in large measure, it is left to the Commission to implement and "flesh out" the actual requirements for separation.

There are several concerns which clearly require the Commission's attention. First, the Commission must ensure that the BOC not be able to defeat the purpose of a separate affiliate by transferring assets to the affiliate or by using the common parent -- presumably a Regional Holding Company -- as a conduit for joint activities or to provide such joint activities itself. Second, the Commission must ensure that the separate affiliate acts "independently" (as required by Section 272(b)(1)). If the separate affiliate is to truly act independently, it must provide service with its own employees, over transmission and switching facilities that it owns or leases, and over its own physical plant. Insofar as possible, it should have the same relationship to the BOC as does an unaffiliated entity. Third, the Commission must ensure (as required by Section 272(b)(5)) that any transactions between the BOC and the separate affiliate are reduced to writing and available for public inspection.

The objective of separation should be to isolate the separate affiliate so that any remaining transactions between the

BOC and the separate affiliate are sufficiently few and sufficiently clear that they can be examined and tested against similar transactions between the BOC and unaffiliated entities. The Commission must be careful to leave as little as possible to the complaint process. There is neither the time nor the resources to engage in multiple, complex adjudications.

The Commission also raises the question as to whether the separate affiliate itself should be treated as dominant. If all else went as planned, and the Commission could ensure that the separate affiliate would not be the beneficiary of discrimination or that it would not take part in anticompetitive activity together with the BOC, there would be no need to classify it as dominant. However, there is an enormous amount that is unknown here and, as the Commission itself recognizes, the dangers to competition are quite serious. Sprint therefore suggests that at least for an initial period, a BOC Section 272(a) affiliate be considered to be dominant. If it turns out that this is unnecessary, such classification can be easily removed -- far more easily than it can be imposed.

Sprint does not discuss in this pleading any issues relating to the modification or removal of the *Competitive Carrier V* separation requirements for independent LECs. The Commission has

delayed the comment date for independent LEC issues to August 29 and Sprint will comment at that time.² All of Part III to Title II is by its terms applicable only to the BOCs. Unlike Section 251, the separate affiliate and other separation requirements adopted in Sections 271 and 272 do not apply to independent LECs and have no relevance -- in terms of precedence or otherwise -- to independent LECs. Even the largest independent LEC, GTE, which is approximately three times the size of the next largest independent LEC (Sprint), was specifically relieved of the obligation to provide interLATA service only through a separate affiliate by the 1996 Act (see Section 601(a)(2)). The dichotomy drawn by Congress between the separation requirements required for the BOCs and the absence of any similar separation requirements for the independent LECs, can hardly be considered surprising. The problems posed by BOC entry into the interLATA market, the possible extent of cross-subsidization, and the possible harm to in-region interLATA competition, have been understood since the AT&T divestiture itself. As compared to independent carriers, the BOCs have substantially greater size and economic power, they have much larger and contiguous serving

² See Order DA 96-1281, released August 9, 1996.

areas, and they serve, almost without exception, the largest urban markets. To use an example close to home, any conceivable threat presented by Sprint's widely dispersed and largely rural telephone companies³ can hardly be likened to that presented by either Bell Atlantic or NYNEX or even less by a combination of these two Regional Holding Companies which stretches unbroken from Maine to Virginia and includes within its borders the entire megalopolis of the Eastern Seaboard.⁴ For these reasons, the DOJ has twice found that Sprint's entry into the interLATA market

³ The court in *United States v. GTE Corp.* recognized that dispersion had "substantial consequences in terms of monopoly control" which meant that "[t]he effect on potential competition of a local-long distance consolidation is likely to be quite different" 603 F.Supp 730, 734 (D.D.C. 1984). The Court also compared the Bell Regional Holding Companies to GTE directly, stating

Each of the Bell regional companies has a very strong, dominant position in local telecommunications in the area in which it serves; GTE's operations, by contrast, are widely scattered. Moreover, the Regional Holding Companies also have the facilities to provide all the intercity and inter-LATA traffic throughout their regions, while the GTE Operating Companies control little by way of intercity facilities, and what facilities they do have are by and large of the entrance type which do not cover the areas in which the companies operate.

603 F. Supp. at 737 (footnote and citation omitted).

⁴ Compare *United States v. GTE Corp.*, *supra*, holding that the GTE acquisition of SPCC and SPSC should not be barred and that the interLATA restrictions placed on the BOCs were inappropriate for application to GTE in part because "[d]ifferent standards are appropriately applied where there is this great a difference in size." 630 F.Supp. at 734 (fn. omitted).

would not cause significant harm.⁵ In contrast, neither Bell Atlantic, nor NYNEX, nor any other BOC has been permitted to enter the interLATA market (even out-of-region) until the passage of the 1996 Act.

II. SCOPE OF THE COMMISSION'S AUTHORITY

In this section of the *NPRM*, the Commission has tentatively concluded that, for purposes of implementing Sections 271 and 272 of the Act, it has authority over both interstate and intrastate interLATA services and interLATA information services (§21), and over all manufacturing activities, since manufacturing cannot be segregated into interstate and intrastate portions (§30). Sprint agrees with both conclusions.

Sections 271 and 272 prescribe regulations for BOC entry into the interLATA services market generally. As the Commission noted, neither of these sections differentiates along interstate/intrastate lines (§22), and when read in conjunction with other Sections of the Act, Sections 271 and 272 seem to assume Commission jurisdiction over both interstate and intrastate interLATA services (§24). The state/interstate service distinction which prevailed under the 1934 Act, under which the states and the FCC each retained "horizontal" authority over intrastate

⁵ First, when US Sprint was formed in 1986 and, second, when it merged with Centel in 1993.

and interstate service respectively, has been replaced with a new regulatory paradigm under which both federal and state commissions share "vertical" responsibility for (among other things) regulating interLATA services. Under the new law, the Commission has jurisdiction over services regardless of whether the traffic would have been interstate or intrastate interLATA under the 1934 Act.⁶

Commission jurisdiction over both interstate and intrastate interLATA BOC services certainly does not eliminate or undermine the states' involvement in the regulation of such services. Under Section 271(d)(2)(b), for example, the Commission is required to "consult with the State commission of any State that is the subject of the application [for the BOC to provide in-region interLATA services] in order to verify the compliance of the Bell operating company with the requirements of subsection (c)" (the competitive checklist). Under Sections 272(d)(2) and 272(d)(3), state commissions will review and verify audits of

⁶ As the Commission stated in its *Interconnection Order*, Sections 251 and 252 of the 1996 Act:

...address both interstate and intrastate aspects of interconnection, resale services, and access to unbundled elements. The 1996 Act moves beyond the distinction between interstate and intrastate matters that was established in the 1934 Act, and instead expands the applicability of national rules to historically intrastate issues, and state rules to historically interstate issues.

Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order released August 8, 1996, ¶24.

Bell operating company transactions with its affiliates to ensure compliance with the nondiscrimination safeguards contained in Section 272.⁷ Thus, the states will continue to play a key role -- particularly in the gathering and analysis of information necessary to evaluate BOC claims that they have satisfied the competitive checklist -- in the regulation of interLATA (both interstate and intrastate) services.

III. ACTIVITIES SUBJECT TO SECTION 272 REQUIREMENTS

In this section of the *NPRM*, the Commission has requested comment on the separate affiliate and nondiscrimination safeguards contained in Section 272.

A. Jurisdiction Over International Services (§32)

The Commission tentatively concludes that the Section 272 requirements apply to a BOC's provision of both domestic and international interLATA telecommunications services that originate in a BOC's in-region states (§32). Sprint agrees. Section 272 speaks to interLATA services generally and does not differentiate between domestic and international telecommunications services. Section 3.21 defines interLATA service as "telecommunications between a point located in a local access and transport area and a point located outside such area" -- a definition which

⁷ The Commission should be aware, however, that many states lack the kind of cost allocation rules that the Commission has adopted in CC Docket No. 86-111.

clearly encompasses international communications. Thus, it is reasonable to conclude that Congress intended to subject all interLATA traffic -- both international and domestic -- to the separate affiliate and nondiscrimination safeguards contained in Section 272.

B. Number of Separate Affiliates Required (§33)

The Commission also tentatively concludes that a BOC may, "if it chooses, conduct all, or some combination, of its manufacturing activities, interLATA telecommunications services, and interLATA information services in a single separate affiliate, as long as all the requirements imposed pursuant to the statute and our regulations are otherwise met" (§33). Assuming that a single affiliate truly is separate from the BOC and the parent RHC, and that adequate accounting separation is implemented,⁸ Sprint does not disagree with the Commission's tentative conclusion here. The statute requires the separation of the local and exchange access service operations of a Bell Operating Company on the one hand, and its manufacturing activities, originating interLATA telecommunications services (except as specified), and interLATA information services (other than electronic publishing and alarm

⁸ As discussed in Section VIII below, it may be that the separate affiliate will need to be classified as dominant in its provision of telecommunications services, depending upon the stringency of the specific structural and accounting safeguards which are adopted.

monitoring services), on the other hand. It does not require establishment of three separate affiliates.

C. Applicability of Section 272(h)

In paragraphs 34 and 39 of the *NPRM*, the Commission has sought comment on the relationship between Sections 272(h), 271(f), and 272(a)(2) of the Act.⁹ Section 272(a)(2)(B)(iii) allows the BOCs to provide any interLATA telecommunications services allowed under the MFJ and MFJ waivers on an unseparated basis. There is no time limit on this exemption. Because there are no separate affiliate requirements with which the BOC must comply in order to provide Section 271(f) interLATA telecommunications services, Section 272(h) does not apply.¹⁰ The one-year deadline imposed in Section 272(h) would appear to apply only to

⁹ Section 272(h) provides that:

With respect to any activity in which a Bell operating company is engaged on the date of enactment of the Telecommunications Act of 1996, such company shall have one year from such date of enactment to comply with the requirements of this section.

Section 272(a)(2) provides in part that the activities described in 271(f) -- those allowed under the AT&T Consent Decree -- are not subject to the separate affiliate requirement.

¹⁰ Some activities of the Regional Holding Companies previously authorized by the court under the now-superseded AT&T Consent Decree were required to be provided in corporate subsidiaries totally separate from the BOC. See e.g., *U.S. v. Western Electric Company, Inc., et al.*, Civ. No. 82-0192-HHG, filed August 8, 1990 (permitting Bell Atlantic and Ameritech to acquire a substantial interest in Telecom Corporation of New Zealand Limited). To the extent that a separate subsidiary was required prior to passage of the Telecommunications Act of 1996, Section 271(f) plainly requires that such activities remain "subject to the terms and conditions contained in" the court's orders.

interLATA manufacturing activities, interLATA information services, and specified incidental interLATA services (Section 272(g)(4)) provided by the BOC. Thus, a BOC may provide the interLATA telecommunications services allowed under the AT&T Consent Decree on an unseparated basis unless and until the Commission rules otherwise (based on misconduct or for any other valid reason).¹¹ Any manufacturing activities, interLATA information services, and incidental interLATA information storage and retrieval services allowed under the MFJ and MFJ waivers may be provided on an unseparated basis for one year from the enactment of the 1996 Act. After that year, these latter services will have to be provided by a separate affiliate and comply with all pertinent nondiscrimination safeguards.

D. Mergers and Joint Ventures (§40)

To date, two pairs of BOCs have announced their intention to merge their operations. Other BOCs may enter into joint ventures with each other to provide interLATA services. Since the BOCs involved in either of these partnership arrangements would have an incentive to discriminate in favor of their prospective partner's affiliates, the Commission has requested comment on what safeguards can or should be implemented.

¹¹ However, these services would be treated as non-regulated services for purposes of cost allocation.

Sprint agrees that in-region states of a merged BOC entity should include all of the in-region states of each of the BOCs involved in the merger. Sprint also recommends that BOC inter-LATA activities involved in or affected by a pending merger or joint venture arrangement should be subject to the same structural and nondiscrimination safeguards as apply to any individual BOC's provision of interLATA services. For example, all of the states in which the pending merger or joint venture partners offer originating service should be treated as in-region states; the BOCs should be required to provide any facilities or services used by a partner's affiliate on an arm's length basis (e.g., at generally available rates, terms and conditions); any preferential joint marketing between the BOC, the BOC's affiliate, the partner, and the partner's affiliate should be prohibited; no BOC should be allowed to pledge its assets to secure credit for its partner's affiliate; and the BOC should be required to file the same type of installation, maintenance, quality of service, etc., reports for facilities and services provided to a partner's affiliate, as apply to the BOC's own affiliate. Without these measures, the BOCs involved could enter into informal partnership arrangements which allow them to provide service to their partners and their partners' affiliates at preferential or anticompetitive rates, terms and conditions,

while bypassing structural and accounting safeguards and essentially escaping vital regulatory oversight.

E. Information Services (§§41-54)

The Commission tentatively concludes (§41) that because the 1996 Act does not distinguish between in-region and out-of-region interLATA services, the BOCs must provide all interLATA information services through a separate affiliate. Sprint agrees. Congress was clearly aware of the distinction between in-region and out-of-region services, having made specific provision for such distinction as regards interLATA telecommunications services. The fact that no such distinction was drawn in Section 272(a)(2)(C) for interLATA information services must be interpreted to mean that Congress intended this section to apply without distinction to interLATA information services.

The Commission has asked what services are included in the statutory definition of information services (§42). Sprint believes that all of the services classified as enhanced by the Commission (see Section 64.702(a) of the Commission's Rules) and provided by the BOCs under their various CEI/Computer III authorizations should be considered information services for purposes of implementing Section 272 of the Act. These enhanced services -- which include voice mail,¹² electronic mail, protocol

¹² Voice mail services fall within the Act's definition of telemessaging services. Telemessaging services generally, like voice mail services

Footnote continues on next page.

processing (including protocol conversion and information storage), interactive voice and data services, and audiotext and videotext gateway services -- all involve the "capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications..." (Section 3.20 of the Act).

Given the pace of technological innovation, it makes little sense to try to list all future applications which might be considered an information service. Instead, the Commission should continue to rely upon its definition of enhanced services and the 1996 Act's definition of information services to evaluate whether or not a service offered by a BOC must be offered by its separate affiliate. In the event that there is some dispute as to whether a new BOC offering is in fact an information service subject to the structural and nondiscrimination safeguards of the Act, the BOC should request an interpretation as to the service's regulatory status from the Commission.

The Commission has also asked how it should distinguish between interLATA and intraLATA information services, since the separate affiliate requirements apply only to interLATA information services (§44). As a practical matter, it is impossible to make this distinction for many information services. For exam-

specifically, should all be classified and treated as information services (see *NPRM*, §54).

ple, callers can send and retrieve voice and electronic mail messages, or access other enhanced services through a BOC gateway, by using remote access features. Therefore, a BOC (or any other information service provider) cannot readily segregate interLATA and intraLATA use of its information service when the service is being rendered. This leaves the Commission with no alternative than to classify as an interLATA information service any information service "that potentially involves an interLATA telecommunications transmission component" (*id.*). Such classification is also more logical and workable than one based upon the locations of a BOC's non-transmission computer facilities and its information service subscriber (§45). It seems unlikely that a BOC would find it economic (or rational from a marketing perspective) to structure its information service offerings based upon whether such facilities are located in a different LATA from a particular end user.

Finally, the Commission has tentatively concluded that it should continue to enforce its existing Computer II, Computer III and ONA unbundling and interconnection requirements to govern the BOCs' provision of intraLATA enhanced/information services (§49) (to the extent that the intraLATA/interLATA distinction can be made for information services). Sprint agrees. To date, the Commission's ONA rules have not been particularly effective at fostering a competitive enhanced services market. Few, if any

unaffiliated enhanced services providers (ESPs) have purchased any of the ONA services offered by the BOCs in their interstate access tariff, primarily because it is financially infeasible to use those ONA elements in conjunction with feature group access. However, it is possible that when the Commission reforms its system of interstate access charges, basing access charges at their economic cost, ESPs may find it more economic to use ONA elements. Since the BOCs already have in place the administrative systems for complying with the Commission's ONA requirements, there is little harm to retaining these requirements in anticipation of future ESP use under a reformed access charge regime.

IV. STRUCTURAL SEPARATION REQUIREMENTS OF SECTION 272

Next to the development of significant, facilities-based local competition, Sprint believes that adequate structural separation requirements offer the best means of ensuring against competitive harm and cross-subsidy that can damage BOC monopoly ratepayers. As already noted, these dangers are inherent in BOC entry into interLATA markets. In order to be effective, structural separation must not only prevent the BOC from engaging in extensive common activities with its Section 272 affiliate but must also prevent the BOC from using its parent (or equivalent) as a conduit to engage in such common activities. By limiting

the extent of sharing among the various pieces of the overall BOC enterprise, the transactions between those pieces that do occur will be limited in type and number. As such, they are more easily visible and auditable by third parties, including the Commission.

Sprint therefore agrees with the Commission that it should interpret the words "operate independently" in Section 272(b)(1) as imposing requirements beyond those listed in the other subsections, especially in light of Section 272(b)(5)'s requirement that all transactions between the Section 272 affiliate and the BOC be at arm's length, in writing and available for public inspection.

In *United States v. GTE Corp.* (*supra* n. 3), and in the Commission's parallel ruling,¹³ the Court and the Commission permitted the acquisition¹⁴ by GTE Corp. of Sprint's long distance predecessors in interest¹⁵ subject to conditions requiring separation. These cases thus provide useful guidelines

¹³ See *GTE Corp.*, 94 FCC 2d 235, 54 RR 2d 161 (1983).

¹⁴ GTE ultimately disposed of SPCC, and the Telecommunications Act of 1996 later vacated that Consent Decree.

¹⁵ These predecessors were the Southern Pacific Communications Company (SPCC) and the Southern Pacific Satellite Company (SPSC).

in determining the meaning of the words "operate independently" in the context of BOC entry into the interLATA business.

The GTE court acknowledged the dangers presented by a powerful monopoly entering the interexchange business. It stated that the case was "a close one, and the Court has reached its decision [approving the acquisition] only because of the strictness and firmness of the decree's injunctive and separate subsidiary provisions." 603 F.Supp. at 737.¹⁶ The Commission likewise based its approval of the GTE acquisition in part on these provisions. 54 RR 2d at 171, 175. Sprint urges the Commission to adopt the tools in those decisions to the extent that the Congress has not explicitly decided otherwise.

In particular, Sprint believes Section 272 should be interpreted to mean that the interLATA affiliate must obtain any transmission and switching facilities it receives from the BOC (or any affiliated Section 251(c) carrier) under generally available rates, terms and conditions and that the shared ownership of such facilities will not be permitted. This was a

¹⁶ These provisions were contained in a consent decree negotiated between the Government and GTE Corp. See *U.S. v. GTE Corporation*, Civ. No. 83-1298, filed December 21, 1984.